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May 16, 2006

AGENDA ITEM 10

TO: MEMBERS OF THE HEALTH BENEFITS COMMITTEE

I. SUBJECT: First Reading – Blue Shield of California – Three-Year HMO Contract Renewal

II. PROGRAM: Health Benefits

III. RECOMMENDATION: Information Only

IV. INTRODUCTION:

The current 3-year contract with Blue Shield of California (Blue Shield) as the exclusive CalPERS Health Benefits Program HMO network plan expires on December 31, 2006. At the May 16, 2006, Health Benefits Committee meeting, representatives from Blue Shield will present and distribute a proposed 3-year business plan to demonstrate the value of a continued partnership and multi-year contract.

V. BACKGROUND:

In June 2002, the CalPERS Board voted to eliminate two major health plans and consolidate its network HMO membership with Blue Shield of California effective January 2003. As a result of this decision, CalPERS saved an estimated \$77 million in premiums for 2003. As was CalPERS usual practice at the time, the Blue Shield contract award was for one year on a fully insured basis. Because pricing for 2004 must occur in 2003, Blue Shield had little or no claims data for nearly 350,000 new members (75% of their CalPERS membership), causing a high degree of uncertainty in its pricing estimates. In the absence of reliable claims experience, Blue Shield's initial conservative assumptions resulted in a proposed overall Blue Shield Basic Plan rate increase of nearly 37% for 2004. Because it was not in the best interest of CalPERS to eliminate another health plan and since the prospect of annually bidding and moving members between plans was great, CalPERS and Blue Shield developed a risk sharing "partnership model" that ultimately resulted in a Basic Plan premium increase of 18.44% for 2004. Simultaneously, Blue Shield was awarded a 3-year contract. The foundation for the partnership was established on three guiding principles:

- Transparency – CalPERS has access to detailed HIPAA compliant data elements that increase understanding of health care cost drivers;

- Accountability – CalPERS expects industry standard benchmarking to be used for performance measurement;
- Aligned incentives – CalPERS requires pay-for-performance terms for providers and the health plan ensures that appropriate attention is placed on unit costs, utilization, and improving health status.

The partnership additionally focused on the achievement of several goals:

- Receive the appropriate level of health plan focus to gain control of rising unit costs and utilization trends;
- Gain increased understanding of market dynamics through data transparency;
- Increase price stability for CalPERS network HMO members; and
- Hold the health plan partner accountable for performance.

A crucial provision of the 3-year contract required Blue Shield to offer an HMO benefit in each of the 40 counties that had an existing HMO plan at that time. To accomplish this, Blue Shield had to establish a provider network in 6 Exclusive Provider Organization (EPO) and 10 Direct Contract (DC) counties within a 6-month timeframe.

VI. ANALYSIS:

The following key successes can be attributed to the CalPERS partnership model:

- CalPERS buying power was leveraged with key health care providers by moderating year-over-year price increases.
- The adoption of a hospital narrow network to address hospital costs as a significant expense driver. Nearly \$31 million in savings were realized in 2005; an additional \$42 million in savings is projected for 2006 due to provider efficiency modeling which measures unit costs and provides “credit” for quality improvement initiatives.
- The hospital narrow network was a catalyst for developing the “Partnership for Change” leading the drive for improved and standardized efficiency toward cost effectiveness for California hospitals.

The requirement that Blue Shield offer an HMO benefit in certain EPO and DC counties* is having a substantially negative impact on the overall CalPERS Blue Shield premium. Under a separate agenda item, Blue Shield is proposing actions to mitigate this situation. As our future partner, we expect Blue Shield will continue to use data gathering and analytics to drive decision making and recommendations for improving the CalPERS Health Benefits Program.

Staff has continued discussions and planning with Blue Shield to determine the future benefits of a multi-year contract renewal with CalPERS. Both parties are

* The DC/EPO counties include: Butte, Colusa, El Dorado, Glenn, Lake, Mariposa, Mendocino, Merced, Napa, Plumas, San Luis Obispo, San Mateo, Santa Barbara, Santa Clara, Sierra, and Sonoma

collaborating to ensure stability and viability of future health care benefits. To reach our goals, renewal of the 3-year contract requires Blue Shield to:

- Provide member and provider education to better align benefit design to influence behavior and control health care costs;
- Develop products and price points that are competitive in the market ensuring enrollment, stability, and increase contracting agency participation;
- Continue to evaluate and measure provider efficiency and reward high performance providers, and develop a high efficiency Blue Shield physician network;
- Deliver high-intensity case management programs that control health care costs while ensuring quality for catastrophic cases;
- Deliver disease management programs that help our members with chronic illness gain better control of their own health status;
- Offer an enhanced, customized CalPERS, Health Lifestyle Rewards, that provides incentives for members to get healthy and stay healthy; evaluates the impact of the program on health status and health care cost.
- Take a leadership role in medical record technology to reduce medical errors and improve health care delivery, e.g., the California Regional Health Information Organization (CalRHIO).

Staff is exploring negotiation options with Blue Shield to address specific and measurable goals for the providing of health benefits for another 3-year period. Staff will report back to the Board regarding the status of these negotiations at the June 2006, Health Benefits Committee meeting.

VII. STRATEGIC PLAN:

This item supports Goal X of the CalPERS strategic plan, "Develop and administer quality, sustainable health benefit programs that are responsive to and valued by enrollees and employers." It also supports Goal XI, "Promote the ability of members and employers to make informed decisions resulting in improved lifestyle choices and health outcomes."

VIII. RESULTS/COSTS

This is an information item. Representatives from Blue Shield will make a detailed presentation that will be distributed at the meeting.

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